

IN THE SECOND JUDICIAL COURT OF THE STATE OF NEVADA
IN AND FOR WASHOE COUNTY

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STATE OF NEVADA	:	
	:	
Plaintiff,	:	
	:	
v.	:	
	:	
PHILIP MORRIS, INCORPORATED;	:	No. 9700306
PHILIP MORRIS COMPANIES, INC.;	:	
R.J. REYNOLDS TOBACCO CO.;	:	
RJR NABISCO HOLDINGS CORP.;	:	
RJR NABISCO, INC.;	:	
AMERICAN TOBACCO CO., INC.;	:	
AMERICAN BRANDS, INC.;	:	
LIGGETT & MYERS, INC.;	:	
THE BROOKE GROUP LIMITED; LIGGETT	:	
GROUP, INC.; LORILLARD TOBACCO	:	
CO., INC.; LOEWS CORP.; UNITED	:	
STATES TOBACCO COMPANY; BROWN &	:	
WILLIAMSON TOBACCO CORP.;	:	
B.A.T INDUSTRIES P.L.C.;	:	
BRITISH-AMERICAN TOBACCO	:	
COMPANY, LTD.; HILL AND	:	
KNOWLTON, INC.; THE COUNCIL	:	
FOR TOBACCO RESEARCH - U.S.A.,	:	
INC.; TOBACCO INSTITUTE, INC.,	:	
foreign corporations, and DOES	:	
1 through 50	:	
	:	
Defendants.	:	
-----X	:	

**AFFIDAVIT OF RICHARD DESMOND IN SUPPORT OF THE
MOTION OF B.A.T INDUSTRIES P.L.C. TO QUASH SERVICE OF
THE COMPLAINT FOR LACK OF PERSONAL JURISDICTION**

321223542

UNITED KINGDOM OF GREAT BRITAIN)
 : ss.:
CITY OF LONDON)

RICHARD L. DESMOND, being duly sworn, deposes and says:

1. I am the Group Treasurer of B.A.T Industries p.l.c. ("B.A.T Industries"), and I reside in London, England. I base this affidavit on personal knowledge, except where otherwise noted.

2. I received my M.B.A. from the Harvard Business School in 1964 and was employed at Exxon and Babcock International before joining B.A.T Industries. I have more than twenty years of experience in the treasury function at these companies. I am currently a Fellow of the United Kingdom-based Association of Corporate Treasurers and was President of the Association for the years 1990 and 1991.

3. I have been employed by B.A.T Industries since 1983. At that time, B.A.T Industries was the ultimate parent holding company of several hundred subsidiaries around the world with operations in the tobacco, financial services, cosmetics, paper, packaging, food and retailing businesses. Today, B.A.T Industries' subsidiaries consist principally of companies in the financial services business and companies with tobacco operations, including the Brown & Williamson Tobacco Corporation ("B&W").

4. There has been a long-standing policy at B.A.T Industries to utilize internally generated funds for working capital for the subsidiaries of B.A.T Industries rather than utilize borrowings from third parties. B.A.T Industries also has two subsidiaries that act as additional sources of funding for subsidiaries that undertake major capital investment.

These subsidiaries, B.A.T. International Finance p.l.c. ("BATIF"), a company incorporated in England and Wales, and B.A.T Capital Corporation ("BATCAP"), a Delaware corporation, borrow funds from the world's capital markets. BATIF is primarily a borrower of a variety of currencies in the European capital markets. BATCAP borrows in dollars only, primarily in the United States capital markets. The companies' borrowings in these markets are usually guaranteed by B.A.T Industries. BATCAP and BATIF then lend the funds they have raised in these markets to other subsidiaries of B.A.T Industries. The major benefits of this practice are that (i) it allows subsidiaries of B.A.T Industries to obtain more attractive interest rates based on B.A.T Industries' high credit rating in the public debt markets, (ii) it creates greater efficiency from borrowing directly from capital markets in larger amounts by reducing fees and costs, and (iii) it allows the funding to be handled by a relatively small group of highly qualified staff. Upon information and belief, this practice is common among multinational holding companies.

5. All of the loans provided by BATIF and BATCAP to affiliates are arm's-length transactions -- they are made at market interest rates, standard fees are charged, the loans are reduced to formal contracts between BATIF or BATCAP and the other B.A.T Industries' subsidiaries, and all loans are the result of negotiation between the parties. This is consistent with the policy of B.A.T Industries that all intra-group charges for royalties, commissions, services and fees be based on the principles of normal commercial practice between independent businesses, and represent arm's-length transactions between separate and distinct entities.

6. I understand that plaintiff contends that the financial structure of B&W is imposed by B.A.T Industries. This is simply not the case. Decisions such as the assumption of debt are based on negotiated agreement between B&W and its corporate parents.

7. I understand that plaintiff contends that because of certain financial dealings by B.A.T Industries, including the structuring of the debt used in connection with the acquisition of Farmers Group, Inc. ("Farmers") in 1988, B&W was rendered insolvent. This is incorrect for several reasons.

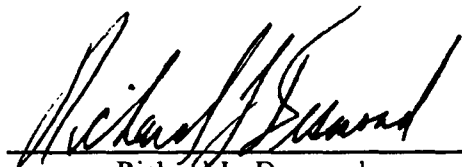
8. First, the allegations that the structure of the Farmers acquisition or its financing were either improper or were somehow aimed at leaving B&W judgment-proof are incorrect and ignore the circumstances surrounding the transaction. The financial dealings of B.A.T Industries and its subsidiaries, including the capital structure related to the acquisition of Farmers, occur within a strict regulatory regime. Intra-group transactions face stringent regulatory requirements and careful review from numerous regulatory agencies including, among others, the Inland Revenue (the United Kingdom tax authority), the United States Internal Revenue Service, the Bank of England, the United Kingdom Department of Trade and Industry and United States insurance regulators. In particular, the acquisition of Farmers was considered and reviewed by insurance commissions in each of the nine states in the United States with jurisdiction in this connection over Farmers, as well as the tax authorities in the United Kingdom and the United States.

9. BATUS Holdings, Inc. ("BATUS"), a subsidiary of B.A.T Industries and a Delaware corporation that was the holding company for all of B.A.T Industries' indirect subsidiaries in the United States, was the company that acquired Farmers. At the time, BATUS owned shares of companies within the United States in retailing such as Saks Fifth Avenue and Marshall Field, and in paper such as Appleton Papers, as well as other companies.

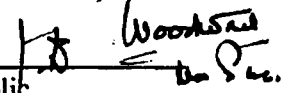
10. In asserting that B&W is insolvent, plaintiff confuses two types of analyses: (i) the net position based on book value of B&W's assets, and (ii) the value of B&W as a going concern, based upon cash flows and fair market value of assets. Plaintiff's reference to "negative equity" relates to the book value of B&W resulting from the artificially low book value of the company's brands, which are maintained at their historical level due to the difficulty inherent in such valuation. B&W's book value is not a reflection of its solvency.

11. By contrast, the solvency of B&W is based upon its cash flow and the fair market value of its assets. B&W is not insolvent and has never been insolvent. It has been, and continues to be, a highly profitable business. For a short period between 1993 and 1994, the cash flow of B&W and the market value of its brands suffered from the adverse impacts of an industry price war triggered by Philip Morris substantially reducing the price of its premium brand cigarette Marlboro on April 1, 1993, a day which has come to be known as "Marlboro Friday." The impact caused by Marlboro Friday on B&W was rectified in October 1994 by way of a capital investment in B&W by B.A.T Industries of \$915 million.

12. I also understand that plaintiff asserts, at page 30 of its Opposition to B.A.T Industries' Motion to Quash, that B.A.T Industries has engaged in "a systematic sequence of asset stripping [from B&W] by way of declaration of" B&W dividends. This allegation is not true. The Board of B&W decides on the dividend payments made to its parent company only after taking into account its own financial needs.


Richard L. Desmond

Sworn to before me this
11 day of March, 1998


Notary Public
England J. D. WOODWARD

Notary Public of London and elsewhere in England

